FILE COPY

FILED
DEC 4 19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1935

No. 26

GEORGE W. McCANDLESS, as Receiver of Duquesne Gas Corporation,

Complainant,

against

MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION, and CHAUCER CORPORATION,

Defendants.

PETITION FOR REHEARING ON BEHALF OF MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION AND CHAUCER CORPORATION, DEFENDANTS BELOW.

LOUIS B. EPPSTEIN,
Counsel for Petitioners.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1935

No. 26

GEORGE W. McCANDLESS, as Receiver of Duquesne Gas Corporation,
Complainant,

against

MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION and CHAUCER CORPORATION,
Defendants.

PETITION FOR REHEARING ON BEHALF OF MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION AND CHAUCER CORPORATION, DEFENDANTS BELOW.

To the Honorable Charles E. Hughes, the Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

The above-named defendants, Maxime H. Furlaud, Kingston Corporation, Byron Corporation and Chaucer Corporation, present this, their petition for a rehearing of the above-entitled cause.

Jurisdiction.

The petition for certiorari in this cause was filed on April 18, 1935, and certiorari was granted on May 13, 1935. This Court rendered its decision on November 11, 1935 reversing the judgment of the United States Circuit Court of Appeals for the Second Circuit and modifying its judgment in other respects.

This petition is filed within less than twenty-five days thereafter under Rule 33 of the General Rules of the United States Supreme Court.

Reasons for Petition for Re-hearing.

The petitioners contend:

I.

That in its consideration of the admissibility of the testimony concerning overvaluation of the property conveyed to Duquesne Gas Corporation and concerning misrepresentations of value made to purchasers of securities of Duquesne Gas Corporation by these promoters, this Court in its majority opinion inadvertently overlooks several important factors.

A. The Court says:

> *"The complaint was based upon the theory that the promoters had been guilty of unconscionable conduct."* (Italics ours.)

There were no facts alleged in the complaint from which any unconscionable conduct could be inferred.

The theory upon which the complaint was based was that every transaction between a promoter and a corporation organized by him, in which the promoter makes a profit as a result of the sale of the securities received by him from the corporation in exchange for property transferred to it by him, is unconscionable.

This, of course, is unsound.

The unconscionable conduct upon which the majority opinion of this Court was based consisted of the claim that an appraisal of the properties conveyed to Duquesne Gas Corporation grossly overvalued the properties so conveyed, and that the representations made by the promoters to the public upon the offering of these securities was to the effect that the appraised value represented the fair market value of these securities.

The complaint did not allege any of these facts, and it is our contention that the evidence tending to establish them was improperly admitted.

The facts actually alleged were that Duquesne Gas Corporation was organized by the promoters who owned all of its stock; that the promoters had acquired options on oil and gas properties in Pennsylvania at a cost of $2,500,000 prior to the organization of the corporation; that prior to actually exercising their options the promoters secured subscriptions from the public for part or all of the bonds and notes to be issued by the corporation; that the promoters thereafter caused the corporation to acquire the properties from them at a price largely in excess of $2,500,000 and issued its bonds and notes to the promoters in payment and that as a result of disposing of the bonds and notes so acquired by the promoters they made a large profit out of the transaction.

There is certainly nothing improper or unconscionable necessarily growing out of that statement of facts. If it be assumed that the property optioned to the promoters had greatly enhanced in value or was worth more than was paid for it, and that the par or stated value of the securities issued was less than the fair value of the property exchanged, no one could justly criticize the transaction.

Certainly, under that state of facts no cause of action could possibly accrue either to the corporation which acquired the properties or to the public who acquired the securities.

Something more than appears in this complaint must be shown to establish a cause of action.

Under the law as it existed prior to this decision:

If the action were one to recover secret profits, it was necessary to show that the promoters were not the sole owners of the stock of the corporation at the time of the transaction and that they practiced a fraud on the other interested parties.

If the action were one brought by a purchaser of the securities, allegations of fraud and misrepresentation of some character were required.

Under the new theory established by this opinion it should be necessary to make allegations in the complaint which would bring the case within such theory.

What we here contend is that this complaint contains no such allegations.

There is no allegation in the complaint as to what was the value on April 7, 1930, the closing date, of the property transferred to Duquesne Gas Corporation.

Nor is there any allegation in this complaint to the effect that any misrepresentations as to the value of the property

acquired by Duquesne Gas Corporation were made to any one. The complaint does not allege that there was an appraisal made or that the appraisal overvalued the property referred to therein or that any such facts were communicated to any one.

There was no allegation in the complaint to the effect that the corporation was either rendered insolvent or that its capital was impaired by these transactions.

The majority opinion of this Court is based entirely upon the assumption that these facts were sufficiently established. That there was in the record evidence tending to establish these facts must be conceded but it was the admission of this very testimony that was so strenuously objected to and concerning which exceptions were not only requested by the defendant but stipulated to by counsel for the plaintiff and formally granted by the Trial Court.

What we here call to the attention of this Court is that testimony was introduced upon the trial of this case (over the most strenuous objections and exceptions of these defendants) tending to show that the value of the property acquired by Duquesne Gas Corporation was less than that at which it had been appraised and that fraudulent misrepresentations had been made to the public concerning its value under a complaint that did not allege any of these facts. The majority decision of this Court is based solely upon this evidence.

Nor is there anything in the laws of Pennsylvania which could be invoked by the plaintiff under this complaint.

Under the Constitution of the Commonwealth of Pennsylvania, securities issued in excess of the *value* of the property conveyed to a corporation in exchange therefor are, under certain circumstances, declared to be void. This

certainly cannot mean that, if the securities were conveyed to the corporation in excess of their cost to the transferor but not in excess of their then fair market value, such securities would be void.

That oil and gas and mining properties rapidly increase and decrease in value is so well known as to be referred to in many decisions upon this subject.

B. The opinion next comments upon our right here to rely upon the exceptions taken in the lower court, notwithstanding the fact that plaintiff three times stipulated that we should have an exception to the entire line of testimony and that the Trial Court, upon the introduction of the very last testimony upon this subject, formally stated in his last ruling upon this subject that the defendants "may have an exception to this line of testimony" (R. 113).

The opinion says:

> *"To this it may be added that the trial judge received the testimony provisionally and subject to a motion to strike out when all the evidence was in. The motion was not made."* (Italics ours.)

We respectfully insist that this Court has inadvertently overlooked certain very vital facts in connection with the admission of this testimony. It is true that after the first objection to the admissibility of this line of testimony was made, and an exception duly taken, some discussion occurred and the Trial Judge stated that he would take the testimony for the present but would later entertain a motion to strike it out (R. 60).

But as the case proceeded the defendants so often and so persistently objected, claimed surprise, and told the Court

that they were not prepared to proceed with the trial upon the theory presented by this line of inquiry (R. 57-60, 61, 62, 63, 109, 113) that, finally, the plaintiff on three different occasions stipulated in open court that the defendants should be held to have an exception to this entire line of testimony (R. 53, 54, 63).

Moreover, at the very end of plaintiff's case, in fact when the very last question on this subject asked of any witness was put to Charles C. Nuss concerning the value of certain tracts included in the appraisal, a final objection was made, whereupon the Court, after granting an exception to the admission of that testimony, said:

> "Yes, you may have an exception to this line of testimony" (R. 113).

Under these circumstances was a motion to strike out required of these defendants?

We do not think that a motion to strike out testimony admitted over objection, argument and exception such as took place in this case has ever been required. Of course, where testimony has been received provisionally subject to a motion to strike it out at the end of the trial and *where no exception has been taken to the ruling of the court at the time of its admission,* failure to make such motion leaves the testimony in the case. The reason for this rule is obvious, particularly if the testimony so admitted involved issues that could be cured by amendment of the complaint without prejudice to the parties.

In this case, however, the defendants objected to the introduction of testimony along these lines so persistently as to cause counsel for defendants to feel that further argument or persistence on this subject would simply result in

annoyance to the Court. This was the more true because counsel for plaintiff had, as we have shown, three times stipulated that defendants should have an exception to this entire line of testimony, but finally at the very end of plaintiff's case defendant again called the attention of the Court to its position on this subject and the Court stated:

> "Yes, you may have an exception to this line of testimony" (R. 113).

This was the final ruling of the Court upon this subject, and, we respectfully insist, was intended by the learned Trial Court to protect the defendants' rights in this respect and was so accepted by the defendants.

As stated by Judge Sanborn in *Salt Lake City* vs. *Smith,* 104 Fed. 457, at page 470:

> "When a question has once been fairly presented to the trial Court, argued, and decided, and an exception to the ruling has been recorded, it is neither desirable nor seemly for counsel to continually repeat their objections to the same class of testimony, and their exceptions to the same ruling which the court has advisedly made as a guide for the conduct of the trial. Counsel for the city lost nothing by their failure to annoy the Court by repeating an objection which it had carefully considered and overruled."

In *Grand Trunk Pac. Ry. Co.* v. *Tollard* (C. C. A. 8th) 286 Fed. 676, the Court says (p. 678):

> "Nor is it necessary after an objection to the admission of incompetent testimony has been erroneously overruled, to move to strike that testimony, no more so than to repeat objections to a class of evidence, after an objection has once been overruled."

In *Walrath* v. *Hanover Fire Ins. Co.*, 216 N. Y. 220, the Court says at page 225:

> "At the close of the entire evidence the court permitted the plaintiff, under the proper objection and exception of the defendant, to insert in the complaint, as an amendment, allegations to the effect that the defendant agreed to deliver the policy of insurance and had failed and neglected to perform that agreement. The defendant, as we have stated, objected throughout the trial to the admissability of the evidence in proof that the defendant made a parol agreement to insure the plaintiff and violated it. The complaint could be amended only at a time which would give the defendant a right and opportunity to meet by proof the allegations made against it."

See also *Northam* v. *Dutchess Co. Mut. Ins. Co.*, 177 N. Y. 73.

> *In this connection we desire to call attention to the fact that there was never any motion made by the plaintiff to conform his pleadings to the proof.*

He stood upon his pleadings from the beginning. He filed a complaint and then an amended complaint. Nor was he ambushed into this situation. Before any answer was filed, a motion was made to require him to make a further and better statement of his cause of action (R. 13). He refused to do this. He elected to stand upon his complaint then. He elects to stand upon his complaint now.

Counsel for complainant has never questioned the fact that defendants had a valid exception to the action of the Court in admitting this testimony. In his argument in the lower court and in his argument before this court he con-

tended that this testimony was admissible under the complaint as framed. He contended, in effect, that having alleged that the defendants were promoters, therefore trustees, he was at liberty to introduce any testimony showing or tending to show a violation of their duties as trustees even if the ultimate facts showing such violations were not alleged. He contended that the allegation in the complaint concerning the purposes of the issue, whether true or false, created a trust relationship.

We respectfully insist that the orderly administration of justice and the traditions of this court require much more of a complaint. This court has always held that a complaint must contain allegations of the ultimate facts to be relied upon, that it is not sufficient to allege generally that the acts of the defendant were unconscionable or merely that a trustee violated his duty as such. Such allegations are mere conclusions of law and if unsupported by allegations of facts, raise no issue. At least the ultimate facts to be relied upon to establish a charge of unconscionable conduct or a violation of duty must be alleged.

In *Fogg* v. *Blair*, 139 U. S. 118, at page 127, Mr. Justice Harlan, speaking for this Court, says:

> "As he impugned the good faith of the transaction between the company and the contractors, it was incumbent upon him to state the essential, ultimate facts upon which his cause of action rested, and not content himself with charging, generally, that what was done was 'colorable,' a 'fraud,' a 'breach of trust,' and a 'scheme' by which Blair and Taylor were to get the stock without paying for it. These are allegations of legal conclusions merely, which a demurrer does not admit. * * * It is consistent with the allegations of the bill that the stock

> was absolutely without value when issued to Blair and up to the time when the railroad and all the property appurtenant thereto was sold under the decree of foreclosure."

See also:

Aberdeen Bank v. *Chehalis County,* 166 U. S. 440, at page 461-462;
Collins v. *Johnston,* 237 U. S. 502, at page 507.

In *Chamberlain Machine Works* v. *United States,* 270 U. S. 347, Mr. Justice Sanford, speaking for this Court, says (p. 349):

> "The general allegations of 'fraud' and 'coercion' were mere conclusions of the pleader; and were not admitted by the demurrer. To show a cause of action it was necessary that the petition state distinctly the particular acts of fraud and coercion relied on, specifying by whom and in what manner they were perpetrated, with such definiteness and reasonable certainty that the court might see that, if proved, they would warrant the setting aside of the settlement. * * * The petition contained no such specific allegations; and since its vague and general averments did not overcome the effect of the release, the demurrer was properly sustained."

There are no allegations in this complaint (except the mere conclusions of law contained in them) which charge any unconscionable conduct on the part of the defendants or any violation of their duties as trustees. The ultimate facts upon which the majority opinion of this court is predicated is that the appraisal of the Duquesne Gas assets was excessive and fraudulent; that the circulars which

Furlaud & Company, Inc. issued in connection with the sale and disposition of the bonds and notes of Duquesne Gas Corporation grossly and fraudulently misrepresented the value of the property by which they were secured.

These facts, however, were never alleged in the complaint nor were there any allegations in the complaint from which it could be inferred that plaintiff intended to rely upon them.

Moreover, even if we had made no objection to the introduction of this testimony and even if no stipulation had been entered into by which it was agreed that we were to have a general exception to this entire line of testimony and even if the Court had not at the end of plaintiff's case confirmed this stipulation by stating to the effect that we may have an exception to this line of testimony, and even if we had not at the end of the case made a motion to dismiss the complaint, we feel that under the tradition of this Court as established by its decisions, in the absence of an amendment to conform the pleadings to the proof, plaintiff could not recover upon those facts.

As stated by Mr. Chief Justice Marshall in *Crockett* v. *Lee*, 7 Wheat. 522:

> "The hardships of a particular case would not justify this tribunal in prostrating the fundamental rules of a court of Chancery—rules which have been established for ages, on the soundest and clearest principles of general utility. If the pleadings in the case were to give no notice to the parties or to the Court of the material facts on which the right asserted was to depend, no notice of the points to which the testimony was to be directed, and to which it was to be limited; if a new case might be made out in proof, different from that stated in the pleadings, all will perceive the confusion and uncertainty

which would attend legal proceedings and the injustice which must frequently take place. The rule that the decree must conform to the allegations, as well as to the proofs of the parties, is not only one which justice requires, but one which necessity imposes on Courts.

In the case of *Garrett* v. *Louisville & N. R. Co.* 235 U. S. 308, at page 312, this Court says:

> "Every bill must contain in itself sufficient matters of fact, *per se,* to maintain the plaintiff's case; and if the proofs go to matters not set up therein the court cannot judicially act upon them as a ground for decision, for the pleadings do not put them in contestation.

As far back as in the case of *Foster* v. *Goddard,* 1 Black 506, this Court per Mr. Justice Swayne said (p. 518):

> "In equity proceedings the proofs and allegations must agree. A party can no more succeed upon a case proved but not alleged, than upon a case alleged, but not proved."

If this line of testimony were inadmissible under the complaint herein, as we think we have demonstrated that it was, how could the plaintiff have amended his complaint at the end of the trial or during the trial so as to render it admissible without at least giving to the defendants full opportunity to answer and to procure evidence to meet it?

If we are right in the foregoing, it indubitably follows that the evidence tending to establish the fact that the property conveyed to Duquesne Gas Corporation was greatly overvalued and that material misrepresentations as to the value of the property were made to the purchasers of securities, under the complaint as filed, should be disre-

garded. That these facts are not alleged in the complaint is too obvious to require argument, and was conceded by counsel for the complainant upon the oral argument before this Court. That the establishment of these supposed facts is essential to plaintiff's right of recovery is demonstrated by the majority opinion of this Court. We have always contended and still do that without the establishment of these facts no cause of action is alleged in the complaint and we believe that both the majority and minority opinions of this Court sustain us in this view.

This Court stresses the fact that the defendants offered no evidence to establish the value of the property conveyed at the time of its conveyance.

We respectfully ask how could the defendants have properly met that issue at that time? The case was on trial and defendants had no notice that that issue existed in the case.

However, it is in evidence that between the acquisition of the options in this case and the closing of the deal, a very large well, producing 7,000,000 cubic feet of gas per day, was brought in on the Nuss property (R. 64). Nuss testified that he was producing 700,000,000 cubic feet of gas a year (R. 60). This well alone would, if it continued to produce at that rate, have furnished the corporation with three times the amount of gas that all of the other wells owned by Nuss had in the past produced. It, doubtlessly, in the opinion of the experts, gave an enhanced value to a large additional acreage. Defendants did not have the expert who made the appraisal available. The preparation of an issue of this kind requires time and research and defendants were not given the opportunity to prepare their case upon this subject. They were never advised that the issue existed.

Again, the report of Barrow, Wade, Guthrie & Co. showed that the very combination of these properties had the effect of enhancing their value to a single corporation operating all of them (R. 194). Before they were combined, they had nine sets of executives, nine selling organizations, and eight independent drilling outfits. After they were combined they had one executive staff, one selling agency, one engineering staff.

We do not contend that this one organization did not cost more than any one of the nine organizations composing the group, but we do insist that the saving was tremendous. To prepare the evidence upon this subject would have required more time than was available to defendants after the case was actually on trial.

There is no question made but that the Duquesne Gas Corporation had ample natural gas to fully supply the requirements of that district of Pennsylvania which it served and that if this market had continued even as it existed in 1929 and 1930, the enterprise would have been completely successful.

This market, as a result of the industrial depression, was so curtailed that the amount of gas sold was hardly sufficient to cover the overhead and depletion charges. But, except in the most general way, this testimony was not available to the defendants. It would have required much time and intensive research to have procured admissible testimony upon this subject. It would have required at least the investigation of the requirement before and after 1930 of the principal customers who were large industrial manufacturers to show not only what the facts were but what were the reasons for the falling off of this market. We are advised that one customer alone, whose normal annual requirements prior to 1931 amounted to approximately two

hundred thousand dollars, used less than fifty thousand dollars of fuel gas in 1931.

What we are here trying to demonstrate is that it would have been impossible at the trial of this case to have properly prepared to meet this issue.

II.

We believe that this Court, in distinguishing this case from the principles of law announced by Mr. Justice Holmes in *Old Dominion Copper Co.* v. *Lewisohn*, 210 U. S. 206, has overlooked certain substantial equities, the consideration of which we now urge upon it.

First, in this case, as in the *Lewisohn* case, the promoters organized their own company, transferred property to it and received in exchange the securities of their own corporation. That the defendants in the case at bar had first felt out the market and determined that they could market the securities so received is true.

That Lewisohn and Bigelow created a market for the stock of the Old Dominion Copper Mining & Smelting Company, and, after disposing of the stock of the corporation, bailed themselves out and made great profits, is also true.

Had these defendants retained these securities, we do not think that any one could have said that any wrong was done to any one. As stated in the *Lewisohn* case:

> "At the time of the sale to the plaintiff, then, there was no wrong done to any one. Bigelow, Lewisohn, and their syndicate were on both sides of the bargain, and they might issue to themselves as much stock in their corporation as they liked in

> exchange for their conveyance of their land" (p. 212).

So, in this case, if there had been no sale of securities to the public there could have been no wrong done to any one. The parties could have issued to themselves as many securities as they liked in exchange for the conveyance of their land. Certainly, there could have been no wrong done to the corporation. The promoters and the corporation were one.

Again, quoting from Mr. Justice Holmes' opinion:

> "If there was a wrong, it was when the innocent public subscribed. But what one would expect to find, if a wrong happened then, would not be that the sale became a breach of duty to the corporation nunc pro tunc, but that the invitation to the public without disclosure, when acted upon, became a fraud upon the subscribers from an equitable point of view, accompanied by what they might treat as damage. *For it is only by virtue of the innocent subscribers' position and the promoters' invitation that the corporation has any pretense for a standing in court.* (Italics ours).

We believe that that is true in this case.

This Court, in the *Lewisohn* case, very definitely suggested that any purchaser of securities would have a personal cause of action against the promoters in the event that any fraud was practiced upon him, but that the corporation would not as the result of such facts have a cause of action.

In considering the equities, it must be remembered that in cases such as this, when a receiver of a corporation is appointed, the market price of its bonds and notes fall to a very small fraction of their original cost to the public and

are picked up by speculators at such prices. Duquesne bonds and notes were at the time of the institution of this suit selling at five, six and seven per cent. of their par value.

So that by the time a suit of this kind comes to this Court for decision the parties who are or were interested in such securities naturally fall into three classes—first, those original subscribers of securities who held them from the beginning, second those purchasers of securities who bought them at high prices but who were compelled to or did part with them at a fraction of that cost, and third, speculators, who after the appointment of the receiver, purchased these securities at a small fraction of their cost.

As to the first class, they have their cause of action against the promoters from whom they can secure complete indemnity for the wrong done them; but under this decision they secure indemnity a second time and thereby subject these promoters to a double liability for the same act. As to the second class, they of course have their cause of action against the promoters and are entitled to secure full indemnity, but by reason of the fact that they have disposed of their securities they receive no additional benefits under this decision.

As to the third class, they have no cause of action against the promoters. They are mere speculators and with full knowledge of the situation purchased bonds and notes at extremely low prices. Yet, under this decision, they are unjustly enriched, and, as a result thereof, the promoters are again subject to a double liability; that is to say, the promoters must pay to the members of the second class full indemnity for the wrong which they suffered and the promoters have to pay the third class the same indemnity for wrongs not suffered by them.

Referring for a moment to the stockholders, if they were induced to make any purchases by reason of any false statement made by Furlaud & Company, they have their cause of action and are entitled to secure full indemnity in their individual capacities. But in reorganizations the holders of such equities are practically eliminated.

Here again this decision subjects the promoters to a double liability.

Assuming then that the promoters are able merely to pay the claims of those who may have causes of action against them in their own right, the effect of this decision would seem to us to deprive the second class of purchasers and the stockholders of substantial rights by rendering their debtors financially unable to pay them in full, and to unjustly benefit the first class, and the speculators who had purchased their securities for a song.

We believe that this Court may upon further consideration come to the conclusion that any party who was injured by any false valuation of the property conveyed to Duquesne Gas Corporation should be permitted to vindicate his own rights in a direct proceeding brought by him for that purpose rather than through the instrumentality of this action which gives to one class of litigants the right to recover twice the amount of indemnity to which it is entitled, to another class a profit to which it is not entitled and to a third class no indemnity whatever except such as it can secure by independent proceedings. This decision has the effect of making his recovery in independent actions much less valuable than if this decision had not been rendered, and, in addition, imposes on these promoters double liability for the same wrongs.

We do not believe that this court will seriously doubt that the parties who were injured or thought that they

were injured by the acts of these promoters or by other promoters similarly situated have vindicated or can and will vindicate their own rights.

Moreover, this decision does not and cannot protect the promoters from suits of this character. It merely has the effect of subjecting the promoters to the necessity of twice paying for the damages which they may have caused if they are able to do so.

Nor do we think that viewing the situation from its equitable and practical aspects this Court will assume that promoters of this character will be able to respond to the double liability imposed upon them by this decision. What we are trying to make clear is that the rule embodied in this decision must have the effect of unjustly enriching speculators who have purchased their bonds or notes with full knowledge of all the facts and, to that extent, destroy the rights of purchasers of bonds, notes and stock who may have just causes of action against promoters, who by this rule are rendered unable to meet such just claims.

Moreover, we feel impelled to call the attention of this Court to the following additional facts concerning the stock of Duquesne Gas Corporation.

This stock was all stock without par or nominal value. The original block of 1,000 shares of this stock was purchased by Furlaud & Company, Inc. for 50 cents per share. At that time they were the sole stockholders of the corporation.

A second block of 139,000 shares was sold to Furlaud & Company at 50 cents a share. It still was the sole stockholder of the corporation. Assuming that the remaining stock issued—535,000 shares having no par value—was issued without consideration of any kind to Furlaud & Com-

pany or its agent, how could that transaction have injured Duquesne Gas Corporation? Prior to the issuance of this stock Furlaud & Company owned all of the equity represented by stock in that corporation—Duquesne Gas Corporation had no other stockholder. After that transaction Furlaud & Company still owned all of the equity represented by stock in that corporation. The position of the corporation was not in the slightest degree altered. Before that occurred, all of the stock of the corporation belonged to identically the same interests as it did after the stock was issued. If this transaction had not taken place and Furlaud & Company had caused the stock of the corporation owned by it to be split up into 675,000 shares of stock without nominal or par value, how could that transaction have injured Duquesne Gas Corporation? Whatever equity there was in that corporation was represented by stock and belonged to Furlaud & Company, just as fully before the issuance of the stock to Kingston Corporation as it did afterwards. Nothing resulted from this transaction that could have affected Duquesne Gas Corporation either injuriously or beneficially. The stock ownership was merely evidenced by a greater number of pieces of paper which altogether amounted to no more and no less than that which existed before.

In the resale of this stock, injury may have resulted to someone but certainly no injury could have resulted to Duquesne Gas Corporation. The issuance of this stock could not and did not affect its solvency or insolvency. If the purchasers of this stock acquired a cause of action as the result of their purchases, Duquesne Gas Corporation was not in any degree affected thereby.

There is no evidence in this case that any false representations were made to any purchasers of this stock. The

learned Trial Court found as a fact that there was no such evidence (R. 231-232).

If we assume (as is a fact) that a reorganization of Duquesne Gas Corporation took place it is hardly necessary to point out how little the rights of these stockholders would have been considered in such a reorganization.

The value of their causes of action, so clearly recognized in the *Lewisohn* decision, is in effect in part at least taken away from them by this decision, if the effect of this decision should render the promoters insolvent and unable to meet the total obligations asserted against them. The point, however, which we are here urging is that the issuance of additional blocks of stock of no par value by this corporation to its sole stockholder did not and could not have resulted in any injury to it.

III.

Byron Corporation and Chaucer Corporation call this Court's attention to the fact that only 25 per cent. of the stock of each of these corporations belonged to the wives of Mr. Furlaud and Mr. Reuter respectively and that 75 per cent. of the stock of each of these corporations belonged to two other corporations concerning which no testimony was introduced by the plaintiff.

There is no evidence of any kind in this case that any of the stockholders of these corporations were chargeable with any improper conduct or with knowledge of improper conduct, unless a presumption at law exists that the wives of Furlaud and Reuter respectively are charged with knowledge of their husbands' acts. So far as Chaucer Corporation is concerned there is no direct evidence that

it made any sale or received any money as a result of this transaction. The only testimony on this subject is that of Mr. Roger A. McShea, Jr.

He testified (R. 99-100):

> "I did not examine the books of Chaucer Corporation." (R. 95).

Again at page 98 of the Record, he testified:

> "Of course, I did not see any books of any kind or any records as far as Chaucer were concerned."

At page 99 of the Record, the following testimony appears:

> "Q. Mr. McShea, either from conversations with Mr. Parisette or other members of his staff——
>
> Mr. Hirshfield: Whose staff?
>
> Q. (Continued) ——Furlaud & Company, Inc. or Maxime H. Furlaud or Carlos Reuter, talks with Mr. Parisette or other members of that office, examining the Bergen contract, examination of the Furlaud books, Byron books, Kingston books, were you able to construct an account of the sale of any other shares to Bergen & Company other than the 425,000 shares that you have testified about?
>
> A. No, sir.
>
> Q. I am not asking from books alone, I am asking from statements made by Mr. Parisette or otherwise?
>
> A. Those 425,000 shares to Bergen, is all I know of except what was apparently sold by Chaucer.
>
> Q. I am asking you about Chaucer. I am asking you if you have got any information in these examinations relating (fol. 143) to the matter of the sale by Chaucer?

A. Of course, I have the contract, but I believe from that, that Chaucer sold the same number of shares to Bergen that Byron did.

Q. Were any statements made to you by Parisette or others to that effect?

A. No, I don't believe so.

Q. Will you refresh your recollection by reading what I show you here?

A. I just don't know what you mean, Mr. Royall.

Q. Have you read this, '85,000 shares sold to Bergen', where did you get that from?

A. From my assumption, in accordance with the contract, that Chaucer also sold 42,500 shares, I worked this up on that assumption, which was based upon the contract.

Q. You assumed that the contract was performed 50-50, as the contract on its face indicated it was intended to be?

A. Yes, sir.

Q. And that upon that assumption, if it was performed 50-50, as the contract on its face indicated it was intended to be?

A. Yes, sir.

Q. And that upon that assumption, if it was performed 50-50, Chaucer sold another 42,500 shares to Bergen?

A. That is right.

Mr. Hirshfield: I object to that ground of assumption.

Q. I mean that is the best you can testify on that score?

A. Yes."

Recurring to the question of whether or not the wives of Furlaud and Reuter are as a matter of law chargeable with knowledge of the acts of their husbands, not only are

they not so chargeable but on the contrary, the law presumes them to be innocent of any such knowledge and the presumption to that effect must be overcome by affirmative evidence.

In *Gottlieb* v. *Thatcher,* 151 U. S. 271, this Court says (p. 279):

> "The relationship of the parties does not, of and in itself, cast suspicion upon the transaction, or create such a prima facie presumption against its validity as would require the Court to hold it to be invalid without proof that there was fraud on the part of the grantor, participated in by the grantee. This proposition is so well settled that authorities need not be cited in its support."

In the case of *Shultz* v. *Hoagland,* 85 N. Y. 464, the Court of Appeals says:

> "The relationship of assignor and assignee, and their intimacy and friendship, and the preference given to the latter as a creditor prove nothing by themselves. They are consistent with honesty and innocence, and become only important when other circumstances, indicative of fraud, invest them with a new character and purpose, and transform them from equivocal and ambiguous facts into positive badges of fraud" (p. 468).

But there were no other circumstances in this case which imputed guilty knowledge to either Mrs. Furlaud or Mrs. Reuter or to any other stockholders of these corporations.

Moreover, as a matter of common experience it seems extremely unlikely that a husband would confide in his wife anything that would reflect upon his conduct. It is true that the complaint makes certain very definite charges

to the effect that these corporations were mere instrumentalities of Furlaud and Reuter but no evidence was offered tending to establish that fact. We respectfully submit that there is no evidence in this case of that character. At most it is shown that these corporations acquired from Kingston Corporation an option to purchase from that corporation 510,000 shares of Duquesne Gas Corporation Common Stock at 50 cents per share. This was as much as had ever been paid for that stock. They exercised their option and paid for the stock. If Chaucer participated in the sale to John J. Bergen of which there is no evidence, the most that could be said was that it resold at a profit part of the stock purchased. The assumption that any person connected with either of these corporations had knowledge of any fact that would render the transaction improper is based upon pure speculation and is not supported by testimony in this case.

As to Chaucer Corporation there is no direct evidence that it ever received one cent from John J. Bergen. Mr. Bergen is a well known operator. It would have been very easy for the plaintiff to have put him on the witness stand to establish any facts that he desired to establish with reference to the source from which he obtained his stock. But it must also be remembered that Furlaud & Company had 140,000 shares of this stock. As far as Chaucer Corporation is concerned there is no more proof that it actually consummated this deal with Mr. Bergen than that he acquired that stock from Furlaud & Company. There is no direct evidence that he acquired it at all. The only witness who testified on this subject stated that he had not examined the books or records of any kind so far as Chaucer Corporation was concerned, that no one had told him that Chaucer Cor-

poration had received these sums of money and that he merely assumed that it had.

As to both of the corporations, however, we respectfully insist that no evidence of guilty knowledge on their part is disclosed by the evidence.

They were not parties to any transaction with Duquesne Gas Corporation.

If there were any fraud perpetrated upon the ultimate purchasers of this stock it was a fraud participated in by the Duquesne Gas Corporation providing the same representations were made to such purchasers as this Court has found were made to purchasers of bonds and notes. The effect of this decision would seem to give the Receiver of Duquesne Gas Corporation the right to recover sums that could never have been justly due it, at the expense of those to whom those sums were justly due.

If there were any impropriety in the appraisal of the properties transferred to Duquesne Gas Corporation there is no evidence in this case that any stockholders of these corporations had any knowledge of such fact. They acquired their stock in Duquesne Gas Corporation long after it had been issued to Kingston. They paid for it an amount greatly in excess of its value to Duquesne Gas Corporation or to any one else. If they or either of them sold part of the stock so acquired at a profit, it is not contended that in making this sale they made any representations of any kind to any one. Such transaction, if participated in by Chaucer Corporation, was with the broker to whom it is not shown that any representations were made by any one.

As to the right of this corporation or its receiver to recover on behalf of the creditors for stock issued by it for inadequate consideration or no consideration, this Court in the case of *Fogg* v. *Blair, supra,* states:

"It is averred in the bill, and the demurrer admitted, for the purposes of the hearing below, that full and adequate compensation for the work done by Blair and Taylor was $12,000 per mile in the company's first mortgage bonds. Assuming this to be true, if the stock issued to Blair and Taylor was of any considerable value at the time they received it, or if the circumstances attending its delivery to them indicated bad faith upon their part or upon the part of the corporation, different questions would arise from those now presented. But the bill contains no allegation whatever as to the real or market value of the stock. The court cannot say from any facts set forth in the bill as to the condition of the railroads in question, that the stock when delivered to the contractors was worth par, or that it had any substantial value. If, when disposed of by the railroad company, it was without value, no wrong was done to creditors by the contract made with Blair and Taylor. If the plaintiff expected to recover in this suit upon the ground that the stock was of substantial value, it was incumbent upon him to distinctly allege facts that would enable the court—assuming such facts to be true—to say that the contract between the railroad company and the contractors was one which, in the interest of creditors, ought to be closely scrutinized. He seems to have carefully avoided making any allegation as to the real or probable value of the stock, and to have supposed that the court, in the absence of averment or proof to the contrary, would assume that it was worth par or had substantial value."

The entire theory of the complainant in this case and the conclusion that must necessarily follow from the majority decision of this Court is that these additional pieces of paper representing stock in Duquesne Gas Corporation delivered

to Kingston had no value of any kind. If the facts upon which the majority opinion of this Court was based could not have been overcome by evidence, it must follow that the stock issued by Duquesne Gas Corporation was utterly and completely worthless and that no harm to any one could result from the issuance of the additional stock referred to.

There was no evidence in this case that any false representations were made to any purchaser of this stock. Certainly these corporations made none—nor are they charged with knowledge of any fact that would impute knowledge to them. The learned Trial Court found as a fact that there was no such evidence (R. 231-232). We, therefore, must respectfully urge that the issuance of this stock by Duquesne Gas Corporation could have resulted in no injury to it, first because the parties to whom it was issued owned all of the stock equity in the corporation before it was issued and owned no more after they received it, second, because in the re-sale of this stock no misrepresentations were either alleged or proven, and third because under the theory of the decision herein the stock issued had no value.

For the foregoing reasons it is respectfully urged that this petition for a rehearing be granted, and that the judgment of the United States Circuit Court of Appeals for the Second Circuit be, upon further consideration, affirmed.

Respectfully submitted,

LOUIS B. EPPSTEIN,
Counsel for Petitioners.

Certificate of Counsel.

I, Louis B. Eppstein, counsel for Maxime H. Furlaud, Kingston Corporation, Byron Corporation and Chaucer Corporation, the above-named defendants, petitioners herein, certify that the foregoing petition for a rehearing of this cause is presented in good faith and not for delay.

LOUIS B. EPPSTEIN,
Counsel for Petitioners.